

Group Hospitalization and Medical Services, Inc. (“GHMSI”), the District’s non-profit Blue Cross Blue Shield plan, also known as Blue Cross Blue Shield of the National Capital Area, has operated as a nonprofit health insurer in the District since 1939. In addition to providing health insurance to District residents and businesses, GHMSI also sells its products in Montgomery and Prince Georges Counties, Maryland, and in Northern Virginia, north of Route 123. In 1997, GHMSI affiliated with Blue Cross Blue Shield of Maryland, and formed a Maryland-based holding company known as CareFirst, Inc. (“CareFirst”). In 1999 CareFirst, affiliated with Blue Cross Blue Shield of Delaware. All three of the companies are currently organized and operated as nonprofit companies.

On January 11, 2002, WellPoint Health Networks Inc., a California-based for profit health insurer (“WellPoint”), filed an application with the D.C. Department of Insurance and Securities Regulation (“DISR”) seeking permission to convert GHMSI to a for-profit company and acquire its assets. WellPoint also filed similar applications in Maryland and Delaware to convert and acquire their non-profit Blue Cross Blue Shield Plans. WellPoint has offered the three jurisdictions a total of \$1.3 billion for the entire CareFirst entity. If the conversion and sale of GHMSI are approved, the price WellPoint pays to acquire GHMSI and CareFirst assets will accrue to the public, apportioned between the District of Columbia and the other jurisdictions.

The Insurance Commissioners in each of the three jurisdictions must approve WellPoint’s application. In addition, the District’s Corporation Counsel, and the Attorney General of Delaware must review and approve the application before the conversion and acquisition can occur. The Maryland Attorney General may also review the transaction. Accordingly, if any one of the three jurisdictions disapproves the transaction, neither the conversion nor the acquisition will take place. Congress must enact legislation to permit the conversion of GHMSI because GHMSI’s was chartered as a nonprofit corporation by an act of Congress.

As a non-profit entity, GHMSI has no shareholder owners, and its assets are, in effect, held for the benefit of the public and are considered “charitable assets.” The Hospital and Medical Services Corporation Regulatory Act (D.C. Official Code § 31-3501 *et seq.*) requires the Corporation Counsel to ensure that all charitable assets currently held by GHMSI are “adequately protected” as it seeks to convert to for-profit status. The Corporation Counsel must review and act upon the application pursuant to thirteen (13) criteria set forth in the Healthcare Entity Conversion Act (D.C. Official Code § 44-603 (c)) (“Conversion Act”).

In addition to reviewing the application pursuant to certain statutory criteria discussed below, the Corporation Counsel has two core functions to perform in any conversion. First, he must ensure that the charitable assets have been fairly valued. The Corporation Counsel must consider several factors in determining whether the charitable assets have been fairly valued. These factors include whether: (a) GHMSI “will receive reasonably fair value for its assets and whether the market value of those assets has not been manipulated by the actions of the parties in a manner that causes the value of the assets to decrease;” (b) GHMSI exercised due diligence and used a fair and objective process in deciding to sell the company; (c) any conflicts of interest are present; and (d) any person is being enriched by the transaction. Second, the Corporation Counsel must ensure that these assets continue to be used in an appropriate charitable manner. To accomplish this, the Conversion Act requires that if the transaction is approved, an independent charitable trust must receive GHMSI’s charitable assets to be used “for appropriate charitable purposes consistent with the healthcare entity’s purposes or operations in the affected community.” The Corporation Counsel must also ensure that the charitable assets are not placed at unreasonable short-term or long-term risk and that any charitable trust be controlled independently of GHMSI and WellPoint. In their conversion plan, the applicants are required to include a proposed structure for the charitable trust that will, in turn, be evaluated by the Office of the Corporation Counsel (“OCC”) during its regulatory review. Although the applicants omitted this item from their initial filing, they have been instructed to include it in their amended application due August 26, 2002.

In his review of the application, the Corporation Counsel must: (a) determine whether the transaction is permitted by the federal and District laws that are applicable to nonprofit corporations; (b) investigate whether all persons and companies involved in the transaction are in full compliance with federal, state or local laws in every jurisdiction where they do business; (c) determine whether anyone associated with the transaction has been convicted of violating any federal, state, or local law; (d) determine whether WellPoint is financially sound and has the financial and management capacity to operate GHMSI; (e) determine whether any management contract has been fairly valued in the transaction; and (f) determine whether GHMSI has retained a right of first refusal “to permit repurchase of the assets by a successor nonprofit if and when the for-profit entity that results from the conversion is subsequently proposed for sale, conversion, or merger.”

The role of the Corporation Counsel in reviewing the transaction is distinct from, but complementary to, the role played by the Commissioner of DISR. In general terms, the role of the Commissioner of DISR is to ensure that the proposed conversion of GHMSI from a nonprofit to a for-profit company is in the public's interest, that the resulting for-profit company would be a financially viable entity, and that GHMSI's policyholders and the insurance-buying public will not be harmed as a result of the conversion and acquisition. For more information on the role of the Commissioner of DISR, please check DISR's website at <http://disr.dc.gov>. While also cognizant of these concerns, the Corporation Counsel's first duty is the protection of the charitable assets now held by GHMSI and the preservation of those assets for the future use of the public. In summary, OCC and DISR are required by law to work together to ensure that the best possible decisions are made for the people of the District of Columbia with regard to the transaction.

To do his job, the Corporation Counsel will proceed with a review of the financial and legal documents relating to the transaction. The Corporation Counsel will forward several written requests for documents to the applicants and will assemble the documents received as part of the administrative record. Together with DISR, OCC will retain an independent financial advisor to conduct the necessary evaluation of the financial aspects of the proposed transactions. DISR and OCC have received proposals from qualified investment bankers and are in the process of retaining Cain Brothers, an investment banking firm specializing in the health care industry. Outside counsel, Manatt, Phelps & Phillips, LLP, has also been retained to primarily support OCC in its review of the transaction. District law authorizes the DISR and the Corporation Counsel to retain outside legal counsel and other experts, with the cost to be borne by the WellPoint. Additionally, OCC is presently considering whether it will be necessary to retain additional consultants to provide assistance to OCC in its review of certain issues, such as an executive compensation consultant to provide advice regarding the employment contracts of CareFirst executives and a charitable foundation consultant to provide advice on the formation of the charitable trust.

The Corporation Counsel's review of the transaction is a public process. The public is entitled to review all non-confidential documents submitted to OCC by any party. OCC is establishing a document room at the OCC Library at 441 4<sup>th</sup> Street, N.W. Room 1C-S010, that will be available to the public during office hours by appointment. This document room will

contain all public documents related to the transaction. Some of these documents will be available on OCC's website, <http://occ.dc.gov>. The public will also have an opportunity to attend one or more public forum events commencing in late September 2002. During these events, the public may voice their views and concerns regarding the proposed transaction and the final application filed by GHMSI and WellPoint. In December, the Corporation Counsel will conduct a public hearing before making his determination whether to approve or disapprove the conversion. At that hearing, the Corporation Counsel will hear from GHMSI and WellPoint as well as from interested persons who wish to provide testimony. Public notice of the public forum events and the public hearing will be published in advance and on OCC's website. For further information, please check the OCC website at <http://occ.dc.gov> or call Peter Lavalley, OCC Public Information Officer, at (202) 724-5198.